PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED SHAREHOLDER MATTERS

The shares of WorldCom group stock and MCI group stock have been quoted on The Nasdaq National Market under the symbols "WCOM and "MCIT," respectively, since our recapitalization on June 7, 2001. Prior to June 7, 2001, WorldCom, Inc. common stock was quoted on The Nasdaq National Market under the symbol "WCOM." The following table sets forth the high and low sales prices per share of WorldCom, Inc. common stock, WorldCom group stock and MCI group stock **as** reported on The Nasdaq National Market based on published financial sources and the dividends declared per MCI group share for the periods indicated.

	WorldCom, Inc. common stock		WorldCom group stork		MCI gmup stock		
	High	Law	High	Low	High	Low	Dividend declared
2000							
First Quarter	$55.00	$40.63	$ —	$ —	$ —	$ —	$ —
Second Quarter	47.00	35.88	—	—	—	—	—
Third Quarter	49.97	25.25	—	—	—	—	—
Fourth Quarter	30.44	13.50	—	—	—	—	—
2001							
First Quarter	23.50	14.25	—	—	—	—	—
Second Quarter (through June 7, 2001)	21.52	17.25	—	—	—	—	—
Second Quarter (starting June 7, 2001)	—	—	18.10	13.27	22.50	15.02	0.60
Third Quarter	—	—	15.90	11.50	17.22	11.00	0.60
Fourth Quarter	—	—	16.06	11.79	15.40	10.90	0.60

As **of** February 28,2002, there were 2,962,645,459 shares of WorldCom group stock issued and outstanding, net of treasury shares, held by approximately 64,000 shareholders of record, and 118,325,109 shares of MCI group stock issued and outstanding, net of treasury shares, held by approximately 53,000 shareholders of record.

Prior **to** the recapitalization, we did not pay cash dividends on our common stock and we have never paid cash dividends on the WorldCom group stock. The policy of our board of directors is to retain earnings attributed to the WorldCom group to provide funds **for** the operation and expansion of its businesses.

Preferred Stock

In connection with the Intermedia merger, we issued the following series of preferred stock, which are mandatorily redeemable:

	Number of preferred shares authorized, issued and outstanding	Liquidation preference per preferred share	Annual dividend per preferred share	Associated depository shares	Aggregate # of shares convertible at the option of holder	
					WorldCom group shares	MCI group shares
Series D Junior Convertible preferred stock, par value $0.01 per share.	53,724	$2,500	$175	5,372,410	6,905,398	276,215
Series E Junior Convertible preferred stock, par value $0.01 per share.	64,047	$2,500	$175	6,404,690	5,295,766	211,830
Series F Junior Convertible preferred stock, par value $0.01 per share..	79,600	$2,500	$175	7,960,000	4,729,649	189,185
Series G Junior Convertible Participating preferred stock, par value $0.01 per share	200,000	$1,000	$ 70	n/a	5,555,555	222,222

On August 20, 2001, the holder of our Series G preferred stock exercised its right to require us to redeem all of the outstanding Series G preferred stock at par plus accrued dividends, or approximately $200 million in the aggregate.

The Series D, E and F preferred stock are currently redeemable in whole or in part, at our option for cash plus accrued and unpaid dividends at rates commencing with 103%, declining to 100% in 2004 and thercafter for the Series D and E preferred stock and commencing with 104%, declining to 100% in 2005 and thereafter for the Series F preferred stock.

Dividends on the Series D, E and F preferred stock are payable in cash or shares of our common stock, at our election on each July 15, October 15, January 15 and April 15. To date, we have paid these dividends in cash and we expect to continue to pay cash dividends on our Series D, E and F preferred stock.

The Series D, E and F preferred shareholders are generally entitled to one-tenth of a vote per share of Series D, E or F preferred stock on all matters voting together with the WorldCom common shareholders as a single class.

In October 2001, we exercised our option to redeem all of our outstanding Series B Preferred Stock. Prior to the redemption date, substantially all of the holders of our Series B Preferred Stock elected to convert the preferred stock into 0.1460868 shares of WorldCom group stock and 0.005843472 shares of MCI group stock for each share of Series B Preferred Stock held.

In January 2000, each outstanding share of WorldCom Series C $2.25 Cumulative Convertible Exchangeable Preferred Stock was redeemed by WorldCom for $50.75 in cash, or approximately $190 million in the aggregate.

ITEM 6. SELECTED FINANCIAL DATA

Selected Historical Consolidated Financial Data

We derived the selected historical consolidated financial data presented below as of and for the five years ended December 31, 2001 from our consolidated financial statements and related notes, which include the WorldCom group and the MCI group. Our audited consolidated financial statements for each of the years ended December 31, 1999, 2000 and 2001 are included in this Form IO-K. The pro forma net income per share data set forth below give effect to the recapitalization as though the recapitalization had occurred on Janualy 1, 1999.

You should read the selected financial data together with our audited consolidated financial statements and the "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this document. In reading the following selected financial data, please note the following:

- On September 14, 1998 we completed our merger with MCI. The MCI merger was accounted for as a purchase; accordingly, the operating results of MCI are included from the date of that acquisition.
- During the second quarter of 2001, we reached a long-term strategic decision to restructure **our** investment in Embratel. Based on actions taken during the second quarter, the accounting principles generally accepted in the United States prohibit the continucd consolidation of Embratel's results. Accordingly, our equity in Embratel's earnings for 2001 is reported in miscellaneous income.
- Results for 2001 include pre-tax costs of $865 million related to the write-off of investments in certain publicly traded and privately held companies, $23 million as a result of costs associated with the tracking stock capitalization, $207 million associated with domestic and international severance packages and other costs related to our 2001 workforce reductions, and $48 million associated with our proportionate share of a receivables write-down at Embratel.
- Results for 2000 include a pre-tax charge of $93 million associated with the termination of the Sprint Corporation merger agreement, including regulatory, legal, accounting and investment banking fees and other costs, and a $685 million pre-tax charge associated with specific domestic and international wholesale accounts that were no longer deemed collectible due to bankruptcies, litigation and settlements of contractual disputes that occurrcd in the third quarter of 2000.
- In 1998, we recorded a pre-tax charge of $196 million in connection with the Brooks Fiber Properties, Inc. merger, the MCI merger and the asset write-downs and **loss** contingencies. The charge included $21 million for employee severance, $17 million for Brooks Fiber Properties direct merger costs, $38 million for conformance of Brooks Fiber Properties accounting policies, $56 million for exit costs under long-term commitments, **$31** million for write-down of a permanently impaired investment and $33 million related to asset write-downs and **loss** contingencies associated with the Brooks Fiber Properties merger and the MCI merger. Additionally, in connection with 1998 business combinations, we made allocations of the purchase price to acquired in-process research and development totaling $429 million in the first quarter of 1998 related to the CompuServe Corporation merger and the acquisition of ***ANS*** Communications, Inc. and $3.1 billion in the third quarter of 1998 related to the MCI merger.
- In connection with debt refinancings, we recognized in 1997 and 1998 extraordinaiy items of $3 million and $129 million, respectively, net of taxes, consisting of unamortized debt discount, unamortized issuance cost and prepayment fees.
- We adopted the American Institute of Certified Public Accountants' Statement of Position 98-5, "Reporting on the **Costs** of Start-up Activities" as of Janualy 1, 1998. The cumulative effect of

this change in accounting principle resulted in a one-time, non-cash expense of $36 million, net of taxes. This expense represented start-up costs incurred primarily in conjunction with the development and construction of the advanced messaging network of SkyTel Communications, which are required to be expensed as incurred in accordance with this accounting standard.

- During the fourth quarter of 2000, we implemented Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements", or SAB 101, which requires certain activation and installation fee revenues to be amortized over the average life **of** the related service rather than be recognized immediately. Costs directly related to these revenues may also be deferred and amortized over the customer contract life. **As** required by SAB 101, we retroactively adopted this accounting effective January 1, 2000, which resulted in a one-time expense of $85 million, net of income tax benefit of $50 million.

	AI or for Ihe Years Ended December 31,				
	1991	1998	1999	2000	2001
	(in millions, except per sham amounts)				
Operating Results:					
Revenues	$ 7,643	$17,617	$35,908	$39,090	$ 35,179
Operating income **(loss)**	982	(942)	7.888	8,153	3,514
Income (loss) heforc cumulative effect of accounting change and extraordinary items	185	(2,560)	4,013	4,238	1,501
Cumulative effect of accounting change	—	(36)	—	(85)	—
Extraordinary items.	(3)	(129)	—	—	—
Net income **(loss)** applicable to common shareholders	143	(2,767)	3,941	4,088	1,384
Earnings **(loss)** per common share:					
Income **(loss)** before cumulative effect of accounting change and extraordinary items:					
Basic	0.10	(1.35)	1.40	1.46	
Diluted	0.10	(1.35)	1.35	1.43	
Net income **(loss):**					
Basic	0.10	(1.43)	1.40	1.43	
Diluted	0.09	(1.43)	1.35	1.40	
WorldCom group **pro** forma net income per share(1):					
Basic	—	—	0.81	0.88	0.48
Diluted	—	—	0.78	0.87	0.48
MCI group pro forma net income **(loss)** per share(1):					
Basic and diluted..	—	—	14.32	13.52	(0.20)
Dividends declared per MCI **group** share	—	—	—	—	1.80
Wcighted-average shares:					
Basic	1,470	1,933	2,821	2,868	
Diluted	1.516	1,933	2,925	2,912	
Financial Position:					
Total assets.	$24,400	$87,092	$91,072	$98,903	$103,914
Long-term debt	7,811	16,448	13,128	17,696	30,038
Company obligated mandatorily redeemable and other preferred securities	—	798	798	798	1,993
Shareholders' investment	14,087	45,241	51,238	55,409	57,930

(1) The WorldCom group stock and the MCI group stock **pro** forma net income per share calculations were calculated using the two-class method, by dividing the earnings allocated to each series of common stock by the number of shares of that series outstanding **for** the relevant period. The earnings allocated to each series of common stock was determined based on the net income or **loss**

amounts of the relevant group determined in accordance with accounting principles generally accepted in the United States consistently applied. The number of shares of each series prior to the recapitalization was determined by assuming that there were the same number of shares of WorldCom group stock outstanding for the periods as there were for our existing stock and that the number of shares of MCI group stock outstanding for the periods equaled $\frac{1}{25}$ of that amount. For 1999, the WorldCom group share amounts equaled 2,821 million (basic) and 2,925 million (diluted) and the MCI group share amounts equaled 115 million for both the basic and diluted computations. For 2000, the WorldCom group share amounts equaled 2,868 million (basic) and 2,912 million (diluted) and the MCI group share amounts equaled 115 million for both the basic and diluted computations. For 2001, the WorldCom group share amounts equaled 2,923 million (basic) and 2,933 million (diluted) and the MCI group share amounts equaled 117 million for both the basic and diluted computations. The combined financial statements of the WorldCom group and the MCI group do not present earnings per share because the WorldCom group stock and the MCI group stock are series of common stock of WorldCom and because the WorldCom group and the MCI group are not legal entities with their own capital structure.

Selected Historical Consolidating Financial Data

The following schedules present balance sheet, statement of operations and statement of cash flows data of the WorldCom group, the MCI group and WorldCom for each of the three years ended December 31, 2001. We have presented this information to illustrate the financial results of the WorldCom group and the MCI group and how the financial results of these groups relate to the consolidated results of WorldCom. This information, which has been prepared in accordance with accounting principles generally accepted in the United States, should be read together with the audited financial statements of each of WorldCom, the WorldCom group and the MCI group and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this Form 10-K.

The balance sheets, statements of operations and statements of cash flows of WorldCom, the WorldCom group and the MCI group for the years ended December 31, 1999, 2000 and 2001 have been derived from the audited financial statements which arc included in this Form 10-K.

The financial information reflects the performance of the businesses attributed to each of the WorldCom group and the MCI group and includes the attribution and allocation of our assets, liabilities, revenues and expenses between the WorldCom group and the MCI group in accordance with our tracking stock policy, which has been consistently applied for all periods presented, and requires:

- centralized management of most financial activities, under which the MCI group will generally not be allocated any cash balances;
- debt allocated to the MCI group to carry an interest rate equal to the weighted-average interest rate, excluding capitalized interest, of WorldCom plus a spread based upon rates at which the MCI group would borrow if it was a wholly owned subsidiary of WorldCom but did not have the benefit of any guarantee **by** WorldCom. Each group's allocated debt increases or decreases by the amount of any net cash generated by, or required to fund, the group's operating activities, investing activities, dividend payments, share repurchases and other financing activities;
- the MCI group to be allocated an expense for use of our fiber optic systems, which are attributed to the WorldCom group, and the WorldCom group to be allocated an expense for use of our business voice switched services, which are attributed to the MCI group. The fees for each of these services will be equal to a portion, based on usage, of the applicable costs and results in a corresponding decrease in the other group's related depreciation expense;
- the transfer of assets and liabilities between the businesses attributed to one group and the businesses attributed to the other group to he at fair value., and all other material transactions between the groups are intended to be on an arm's-length basis. These other transactions

initially consist of the MCI group's use of buildings, furniture and fixtures and the MCI tradenames, which assets have been attributed to the WorldCom group. The MCI group will be allocated a portion, based on usage, of the applicable costs, which will result in a corresponding decrease in the WorldCom group's related depreciation and amortization cxpcnse;

- the cost of shared corporate services and related balance sheet amounts to be attributed to each of the groups based upon identification of the services specifically benefiting the group. Where determinations based on specific identification are impractical, other methods and criteria are used to make allocations between the groups, such as number of employees and total line costs or revenues generated by each group; and
- the tax expense or benefit allocable to the MCI group to be the amount the MCI group would have incurred had it filed tax returns as a separate taxpayer and the tax expense allocable to the WorldCom group to be the excess, if any, of **our** tax expense over the tax expense or benefit allocable to the MCI group. **Tax** benefits that cannot be used by ***a*** group generating those benefits but can be used on a consolidated basis are credited to the group that generated those benefits.

Our board of directors or any special committee appointed by our board of directors may, without shareholder approval, change the policies set forth in our policy statement. Our board of directors or any special committee appointed by our board of directors also may, without shareholder approval, adopt additional policies or make exceptions with respect to the application of the policies described in **our** policy statement in connection with particular facts and circumstances, **all** ***as*** they may determine to be in the best interests of WorldCom. Our board is subject to fiduciary duties to **all** of WorldCom's shareholders as one group, not to the holders of any series of stock separately. Any changes or exceptions will bc made after a determination by **our** board of what **is** in the best interests of WorldCom as a whole, which may be detrimental to the interests of the holders of one series of stock.

Consolidating Balance Sheet
(In millions)

	At December 31, 1999			
	WorldCom Group	MCI Group	Eliminations(1)	Worldcorn
Current assets	$ 9,037	$ 2,263	$(976)	$10,324
Property and equipment, net	26,227	2,391	—	28,618
Goodwill and other intangibles	37,252	10,056	—	47,308
Other assets	4,717	105	—	4,822
Total assets	$17,233	$14,815	$(976)	$91,072
Current liabilities	$12,694	$ 5,491	$(976)	$17,209
Long-term debt	7,128	6,000	—	13,128
Noncurrent liabilities	5,276	824	—	6,100
Minority interests	2,599	—	—	2,599
Company obligated mandatorily redeemable preferred securities	798	—	—	798
Shareholders' investment	48,738	2,500	—	51,238
Total liabilities and shareholders' investment	$77,233	$14,815	$(976)	$91,072

(1) Represents the elimination of intergroup receivables and payables associated with other intergroup allocations between the WorldCom group and the MCI group. The WorldCom group had a net receivable from the MCI group of $976 million and the MCI group had a corresponding net payable to the WorldCom group.

Consolidating Statement of Operations
(In millions)

	Year Ended December 31, 1999			
	WorldCom Group	MCI Group	Eliminations	WorldCom
Revenues	$19,736	$16,172	$ —	$35,908
Operating expenses:				
Line costs:				
Attributed costs (1)	7,841	6,898	—	14,739
Intergroup allocated expenses (2)	64	189	(253)	—
Selling, general and administrative:				
Attributed costs (I)	2,594	3,113	3,228	8,935
Shared corporate services (3)	1,601	1,627	(3,228)	—
Other intergroup allocated expenses (4)	—	331		
Depreciation and amortization:				
Attributed costs (1)	3,533	821	—	4,354
Intergroup allocated expenses (5)	(520)	(64)	584	—
Other charges	(8)	—	—	(8)
Total	15,105	12,915	—	28,020
Operating income	4,631	3,257	—	7,888
Interest expense	(460)	(506)	—	(966)
Miscellaneous income	237	5	—	242
Income before income taxes and minority interests	4,408	2,756	—	7,164
Provision for income taxes	1,856	1,109	—	2,965
Income before minority interests	2,552	1,647	—	4,199
Minority interests	(186)	—	—	(186)
Net income before distributions on mandatorily redeemable preferred securities	2,366	1,647	—	4,013
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	72	—	—	72
Net income	$ 2,294	$ 1,647	$ —	$ 3,941

(1) Attributed costs rcprescnt costs directly incurred by or attributed to the WorldCom group and the MCI group and do not include any intcrgroup allocations.

(2) The WorldCom group was allocated $64 million for its usage of our business voice switches, which have been attributed to the MCI group, and the MCI group was allocated $189 million for its usage of our fiber optic systems, which have been attributed to the WorldCom group.

(3) Our shared corporate services (such as executive management, human resources, legal, regulatory, accounting and tax, treasury, strategic planning and information systems support) have been allocated to the WorldCom group and the MCI group in the amounts of $1.6 billion and $1.6 billion, respectively.

(4) The MCI group was allocated $303 million of costs related to its use of buildings, furniture and fixtures and $28 million for use of the MCI tradenames, which assets have been attributed to the WorldCom group.

(5) A credit of $492 million and $64 million to depreciation expense has been recorded by the WorldCom group and the MCI group, respectively, to reflect the allocation of a portion of the applicable costs for the **use** by the WorldCom group of the business voice switches attributed to the MCI group, and the proportionate use by the MCI group of the fiber optic systems and buildings, furniture and fixtures attributed to the WorldCom group. Additionally, a credit of $28 million to amortization expense has been recorded by the WorldCom group to reflect the charge to the MCI group for use of the MCI tradenames.

Consolidating Statement of Cash Flows
(In millions)

	Year Ended December 31, 1999			
	Worldcorn Group	MCI Group	Eliminations	WorldCom
Cash flows from operating activities:				
Net income	$ 2,366			$ 4,013
Adjustments to reconcile net income to net cash provided by operating activities	4.986			6,992
Net cash provided by operating activities	7,352			11,005
Cash flows from investing activities:				
Capital expenditures	(7,929)			(8,716)
Acquisitions and related costs	(786)			(1,078)
All other investing activities, net	670			239
Net cash used in investing activities	(8,045)			(9,555)
Cash flows from financing activities:				
Principal repayments on debt, net	(2,894)	—	—	(2,894)
Attributed stock activity of WorldCom, Inc.	886	—	—	886
Intergroup advances, net	2,097	(2,097)	—	—
All other financing activities, net.	(72)	—	—	(72)
Net cash provided by (used in) financing activities	17	(2,097)	—	(2,080)
Effect of exchange rate changes on cash	(221)	—	—	(221)
Net increase (decrease) in cash and cash equivalents	(897)	46	—	(851)
Cash and cash equivalents beginning of period	1,703	24	—	1,727
Cash and cash equivalents end of period	$ 806	$ 70	$ —	$ 876

Consolidating Balance Sheet
(In millions)

	At December 31, 2000			
	WorldCom Group	MCI Group	Eliminations(1)	WorldCom
Current assets	$ 8,092	$ 2,312	$ (649)	$ 9,155
Property and equipment, net	35,111	2,246	—	31,423
Goodwill and other intangibles	36,685	9,909	—	46,594
Other assets	5,939	168	(976)	5,131
Total assets	$85,893	$14,635	$(1,625)	$98,903
Current liabilities	$14,213	$ 4,109	$ (649)	$11,613
Long-term debt	11,696	6,000	—	17,696
Noncurrent liabilities	3,648	2,063	(976)	4,735
Minority interests	2,592	—	—	2,592
Company obligated mandatorily redeemable preferred securities	798	—	—	798
Shareholders' investment	52,946	2,463	—	55,409
Total liabilities and shareholders' investment	$85,893	$14,635	$(1,625)	$98,903

(1) Represents the elimination of intergroup receivables and payables associated with other intergroup allocations between the WorldCom group and the MCI group. The WorldCom group had a net receivable from the MCI group (and the MCI group had a corresponding net payable to the WorldCom group) of $1.6 billion, of which $649 million was classified as current with the remainder classified as long-term.

Consolidating Statement of Operations
(In millions)

	Year Ended December 31, 2000			
	WorldCom Group	MCI Group	Eliminations	Worldcorn
Revenues	$22,755	$16,335	$ —	$39,090
Operating expenses:				
Line costs:				
Attributed costs (1)	8,658	6,804	—	15,462
Intergroup allocated expenses (2)	87	373	(460)	—
Selling, general and administrative:				
Attributed costs (1)	3,682	2,981	3,934	10,597
Shared corporate services (3)	2,007	1,927	(3,934)	—
Other intergroup allocated expenses (4)	—	254	(254)	—
Depreciation and amortization:				
Attributed costs (1)	3,907	971	—	4,878
Intergroup allocated expenses (5)	(627)	(87)	714	—
Total	17,714	13,223	—	30,937
Operating income	5,041	3,112	—	8.153
Interest expense	(458)	(512)	—	(970)
Miscellaneous income	385	—	—	385
Income before income taxes, minority interests and cumulative effect of accounting change	4,968	2,600	—	7,568
Provision for income taxes	1,990	1,035	—	3,025
Income before minority interests and cumulative effect of accounting change	2,978	1,565	—	4,543
Minority interests	(305)	—	—	(305)
Income before cumulative effect of accounting change	2,673	1,565	—	4,238
Cumulative effect of accounting change	(75)	(10)	—	(85)
Net income before distributions on mandatorily redeemable preferred securities	2,598	1,555	—	4,153
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	65	—	—	65
Net income..	$ 2,533	$ 1,555	$ —	$ 4,088

(1) Attributed costs represent costs directly incurred by or attributed to the WorldCom group and the MCI group and do not include any intergroup allocations.

(2) The WorldCom group was allocated $87 million for its usage of our business voice switches, which have been attributed to the MCI group, and the MCI group was allocated $373 million for its usage of our fiber optic systems, which have been attributed to the WorldCom group.

(3) Our shared corporate services (such as executive management, human resources, legal, regulatory, accounting and tax, treasury, strategic planning and information systems support) have been allocated to the WorldCom group and the MCI group in the amounts of $2.0 billion and $1.9 billion, respectively.

(4) The MCI group was allocated $226 million of costs related to its use of buildings, furniture and fixtures and $28 million for use of the **MCI** tradenames, which assets have been attributed to the WorldCom group.

(5) A credit of $599 million and $87 million to depreciation expense has been recorded by the WorldCom group and the MCI group, respectively, to reflect the allocation of a portion of the applicable costs for the use by the WorldCom group of the business voice switches attributed to the MCI group, and the proportionate use by the MCI group of the fiber optic systems and buildings, furniture and fixtures attributed to the WorldCom group. Additionally, a credit of $28 million to amortization expense has been recorded by the WorldCom group to reflect the charge to the MCI group for use of the MCI tradenames.

Consolidating Statement of Cash Flows
(In millions)

	Year Ended December 31, 2000			
	WorldCom Group	MCI Group	Eliminations	WorldCom
Cash flows from operating activities:				
Net incomc.	$ 2,598	$ 1,555	$ —	$ 4,153
Adjustments to reconcile net income to net cash provided by operating activities	2,732	781	—	3,513
Net cash provided by operating activities	5,330	2,336	—	7,666
Cash flows from investing activities:				
Capital expenditures	(10,984)	(500)	—	(11,484)
Acquisitions and related costs	(14)	—	—	(14)
All other investing activities, net	(2,614)	(273)	—	(2,887)
Net cash used in investing activities	(13,612)	(773)	—	(14,385)
Cash flows from financing activities:				
Principal borrowings on debt, net	6,377	—	—	6,377
Attributed stock activity of WorldCom, Inc.	585	—	—	585
Intergroup advances, net	1,592	(1,592)	—	—
All other financing activities, net	(339)	—	—	(339)
Net cash provided by (used in) financing activities	8,215	(1,592)	—	6,623
Effect of exchange rate changes on cash	(19)	—	—	(19)
Net decrcasc in cash and cash equivalents	(86)	(29)	—	(115)
Cash and cash equivalents beginning of period	806	70	—	876
Cash and cash equivalents end of period	$ 720	$ 41	$ —	$ 761

Consolidating Balance Sheet
(In millions)

	At December 31, 2001			
	WorldCom Group	MCI Group	Eliminations(1)	WorldCom
Current assets	$ 8,179	$ 1,926	$ (900)	$ 9,205
Property and equipment, net	36,792	2,017	—	38,809
Goodwill and other intangibles	40,818	9,719	—	50,537
Other assets	6,112	221	(976)	5,363
Total assets	$ 91,901	$ 13,889	$ (1,876)	$103,914
Current liabilities	$ 5,915	$ 4,195	$ (900)	$ 9,210
Long-term debt	24,533	5,505	—	30,038
Noncurrent liabilities	3,742	1,876	(976)	4,642
Minority interests	101	—	—	101
Mandatorily redeemable and other preferred securities	1,993	—	—	1,993
Shareholders' investment	55,617	2,313	—	57,930
Total liabilities and shareholders' investment	$ 91,901	$ 13,889	$ (1,876)	$103,914

(1) Represents the elimination of intcrgroup receivables and payables associated with other intcrgroup allocations between the WorldCom group and the MCI group. The WorldCom group had a net receivable from the MCI group (and the MCI group had **a** corresponding net payable to the WorldCom group) of $1.9 billion, of which $900 million was classified as current with the remainder classified as long-term.

Consolidating Statement of Operations
(In millions)

	Year Ended December 31, 2001			
	WorldCom Group	MCI Group	Eliminations	WorldCom
Revcnucs	$21,348	$13,831	$ —	$35,179
Operating expenses:				
Line costs:				
Attributed costs (1)	8,019	6,720	—	14,739
Intergroup allocated expenses (2)	101	360	(461)	—
Selling, general and administrative:				
Attributed costs (1)	4,052	3,438	3,556	11,046
Shared corporate services (3)	2,006	1,550	(3,556)	—
Other intergroup allocated expenses (4)	—	360	(360)	—
Depreciation and amortization:				
Attributed costs (1)	4,841	1,039	—	5,880
Intergroup allocated expenses (5)	(720)	(101)	821	—
Total	18,299	13,366	—	31,665
Operating income	3,049	465	—	3,514
Interest expense	(1,029)	(504)	—	(1,533)
Miscellaneous income	412	—	—	412
Income (loss) before income taxes and minority interests	2,432	(39)	—	2.393
Income tax expense (bcncfit)	943	(16)	—	927
Income (loss) before minority interests	1,489	(23)	—	1,466
Minority interests	35	—	—	35
Net income (loss) before distributions on mandatorily redeemable preferred securities	1,524	(23)	—	1,501
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	117	—	—	117
Net income (loss)	$ 1,407	$ (23)	$ —	$ 1.384

(1) Attributed costs represent costs directly incurred by or attributed to the WorldCom group and the MCI group and do not include any intergroup allocations.

(2) The WorldCom group was allocated $101 million for its usage of our business voice switches, which have been attributed to the MCI group, and the MCI group was allocated $360 million for its usage of our fiber optic systems, which have been attributed to the WorldCom group.

(3) Our shared corporate services (such as executive management, human resources, legal, regulatory, accounting and tax, treasury, strategic planning and information systems support) have been allocated to the WorldCom group and the MCI group in the amounts of $2.0 billion and $1.6 billion, respectively.

(4) The MCI group was allocatcd $332 million of costs related to its use of buildings, furniture and fixtures and $28 million for use of the MCI tradenames, which assets have been attributed to the WorldCom group.

(5) A credit of $692 million and $101 million to depreciation expense has been recorded by the WorldCom group and the MCI group, respectively, to reflect the allocation of a portion of the applicable costs for the use by the WorldCom group of the business voice switches attributed to the MCI group, and the proportionate use by the MCI group of the fiber optic systems and buildings, furniture and fixtures attributed to the WorldCom group. Additionally, a credit of $28 million to amortization expense has been recorded by the WorldCom group to reflect the charge to the MCI group for use of the MCI tradcnames.

Consolidating Statement **of** Cash **Flows**
(In millions)

	Year Ended December 31, 2001			
	WorldCom Group	MCI Group	Eliminations	WorldCom
Cash flows from operating activities:				
Net income **(loss)**	$ 1,524	$ (23)	$ —	$ 1,501
Adjustments to reconcile net income **(loss)** to net cash provided by operating activities	5,081	1,412	—	6,493
Net cash provided by operating activities	6.605	1.389	—	7.994
Cash flows from investing activities:				
Capital expenditures	(7,619)	(267)	—	(7,886)
Acquisitions and related costs	(206)	—	—	(206)
All other investing activities, net	(993)	(605)	—	(1,598)
Net cash used in investing activities	(8,818)	(872)	—	(9,690)
Cash flows from financing activities:				
Principal borrowings (repayments) on debt, net	3,526	(495)	—	3,031
Attributed stock activity of WorldCom, Inc.	124	—	—	124
Intergroup advances, net	(15)	15	—	—
All other financing activities, net	(555)	(71)	—	(626)
Net cash provided by (used in) financing activities	3,080	(551)	—	2,529
Effect of exchange rate changes on cash	38	—	—	38
Net increase (decrease) in cash and cash equivalents	905	(34)	—	871
Cash and cash equivalents beginning of period	720	41	—	761
Deconsolidation of Embratel	(216)	—	—	(216)
Cash and cash equivalents end of period	$ 1,409	$ 7	$ —	$ 1,416

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

On June 7, 2001, our shareholders approved a recapitalization involving the creation of two separately traded tracking stocks: WorldCom group stock, which is intended to track the separate performance of our data, Internet, international and commercial voice businesses; and MCI group stock, which is intended to reflect the performance of our consumer, small business, wholesale long distance voice and data, wireless messaging and dial-up Internet access businesses.

Through the businesses that we have realigned as the WorldCom group, which have an extensive, advanced facilities-based global communications network, we provide a broad range of integrated communications and managed network services to both U.S. and non-U.S. based corporations. Offerings include data services such as frame relay, asynchronous transfer mode and Internet protocol networks; Internet related services, including dedicated access, virtual private networks, digital subscriber lines, web centers encompassing application and server hosting and managed data services; commercial voice services; and international communications services.

Through the businesses that we have realigned as the MCI group, we provide a broad range of retail and wholesale communications services, including long distance voice and data communications, consumer local voice communications, wireless messaging, private line services and dial-up Internet access services. Our retail services are provided to consumers and small businesses in the United States. We arc the second largest carrier of long distance telecommunications services in the United States. Our services include: basic long distance telephone service, dial around, collect calling, operator assistance and calling card services (including prepaid calling cards) and toll free or 800 services. We offer these services individually and in combinations. Through combined offerings, we provide customers with benefits such as single billing, unified services for multi-location companies and customized calling plans. Our wholesale businesses include wholesale voice and data services provided to carrier customers and other resellers and dial-up Internet access services.

On July 1, 2001, we acquired Intermedia for approximately $5.8 billion, including assumed long-term debt, pursuant to the merger of a wholly owned subsidiary with and into Intermedia, with Intermedia continuing as the surviving corporation and as a subsidiary of WorldCom. As a result of the Intermedia merger, we acquired a controlling interest in Digex, a provider of managed Web and application hosting services. In connection with the Intermedia merger, stockholders of Intermedia received one share of WorldCom group stock (or 57.1 million WorldCom group shares in the aggregate) and 1/25 of a share of MCI group stock (or 2.3 million MCI group shares in the aggregate) for each share of Intermedia common stock they owned. Holders of Intermedia preferred stock, other than Intermedia Series B Preferred Stock, received one share of a class or series of our preferred stock, with substantially identical terms, which were established upon consummation of the Intermedia merger. As a result of the merger with Intermedia, we own approximately 90% of the voting securities of Intermedia.

Since the Intermedia merger, we initiated plans to improve cash flow and operating results by reorganizing and restructuring Intermedia's operations. These plans include workforce reductions and other administrative cost savings, the discontinuance of all product lines with unacceptable or negative margins and the ultimate disposal of all assets associated with such product lines or businesses.

We believe that the Intermedia merger should support our web hosting expansion by providing a comprehensive portfolio of hosting products and services for mid-sized and large businesses. Additionally, we expect that Digex will continue to build its operations and expand its customer base, causing it to continue to incur operating **losses** for the foreseeable future, which could adversely affect our results of operations.

During the second quarter of 2001, we reached a long-term strategic decision to restructure our investment in Embratel. The restructuring included the resignation of certain Embratel board of directors seats, the irrevocable obligation to vote a portion of our common shares in a specified manner and the transfer of certain economic rights associated with such shares to an unrelated third party. Based on these actions, the accounting principles generally accepted in the United States prohibit the continued consolidation of Embratel's results. Accordingly, we have deconsolidated Embratel's results effective January 1, 2001.

The following discussion and analysis relates to our financial condition and results of operations for the years ended December 31, 1999, 2000 and 2001. This information should be read in conjunction with the consolidated financial statements and notes thereto contained herein, and the combined financial statements and notes thereto of each of the WorldCom group and the MCI group contained herein as well **as** the "Cautionary Statement Regarding Forward-Looking Statements" in this Form 10-K.

Additional Discussion Related **to** the **WorldCom Group** and the **MCI Group** Financial Statements

Each of the WorldCom group and the MCI group includes the results of operations shown in the combined statements of operations and the attributed assets and liabilities shown in the combined balance sheets of the relevant group. If we acquire interests in other businesses, we intend to attribute those assets and any related liabilities to our WorldCom group or our MCI group in accordance with our tracking stock policy statement. All net income and cash flows generated by the assets will be attributed to the group to which the assets wcrc attributed and **all** net proceeds from any disposition of these assets will **also** be attributed to that group.

Although we sometimes refer to such assets and liabilities **as** those of the WorldCom group or the MCI group, neither of the groups is a separate legal entity. Rather, **all** of the assets of a group are owned by WorldCom and holders of the WorldCom group stock or the MCI group stock are shareholders of WorldCom and subject to all of the risks of an investment in WorldCom and **all** of its businesses, assets and liabilities.

We intend, **for** so long **as** the WorldCom group stock and the MCI group stock remains outstanding, to include in filings by WorldCom under the Securities Exchange Act of 1934, **as** amended, the combined financial statements of each of the WorldCom group and the MCI group. These combined financial statements will be prepared in accordance with accounting principles generally accepted in the United States, and in the case of annual financial statements, will be audited. These combined financial statements are not legally required under current law or SEC regulations.

Our board of directors or any special committee appointed by our board of directors may, without shareholder approval, change the policies set forth in our tracking stock policy statement. Our board of directors or any special committee appointed by our board of directors **also** may, without shareholder approval, adopt additional policies or make exceptions with respect to the application of the policies described in **our** policy statement in connection with particular facts and circumstances, **all** as they may determine to be in the best interests of WorldCom. **Our** board is subject to fiduciary duties to **all** of WorldCom's shareholders **as** one group, not to the holders of any series of stock separately. Any changes or exceptions will be made after a determination by **our** board of what is in the best interests of WorldCom **as** a whole, which may be detrimental to the interests of the holders of one series of stock. The ability to make these changes may make it difficult to address the future of a group based on the group's past performance.

Results of Operations

The following table sets forth for the periods indicated our statements of operations as a percentage of our revenues for the periods indicated:

	For the Years Ended December 31, 1999	2000	2001
Revenues	100.0%	100.0%	100.0%
Line costs	41.0	39.6	41.9
Selling, general and administrative	24.9	27.1	31.4
Depreciation and amortization	12.1	12.5	16.7
Operating income	22.0	20.9	10.0
Other income (expense):			
Interest expense	(2.7)	(2.5)	(4.4)
Miscellaneous	0.7	1.0	1.2
Income before income taxes, minority interests and cumulative effect of accounting change	20.0	19.4	6.6
Provision for income taxes	8.3	7.7	2.6
Income before minority interests and cumulative effect of accounting change	11.7	11.6	4.2
Minority interests	(0.5)	(0.8)	0.1
Cumulative effect of accounting change	—	(0.2)	—
Net income	11.2	10.6	4.3
Distributions on mandatorily redeemable preferred securities and other preferred dividend requirements	0.2	0.2	0.3
Net income applicable to common shareholders	11.0%	10.5%	3.9%

Year Ended December 31, 2000 vs. Year Ended December 31, 2001

For the years December 31, 2000 and 2001, our revenues were as follows (dollars in millions):

	2000 $	2000 Percent of Total	2001 $	2001 Percent of Total
WorldCom group	$22,755	58.2%	$21,346	60.7%
MCI group	16,335	41.6	13,831	39.3
	$39,090	100.0%	$35,179	100.0%

Reported revenues by category for the years ended December 31, 2000 and 2001 reflect the following changes by category (dollars in millions):

	2000	2001	Percent Change
Commercial Services Revenues			
Voice	$ 7,036	$ 6,591	(6.3)%
Data	7,389	8,620	16.7
International	2,367	2,977	25.8
Embratel, net	3,508	—	(100.0)
Internet	2,455	3,160	28.7
Total Commercial Services Revenues	22,755	21,348	(6.2)
Consumer	7,778	7,227	(7.1)
Wholesale	3,388	2,641	(22.0)
Alternative channels and small business	3,541	2,427	(31.5)
Dial-up Internet	1,628	1,536	(5.7)
Total	$39,090	$35,179	(10.0)

Commercial services revenues, which include the revenues generated from commercial voice, data, international and Internet services, for 2001 were $21.3 billion versus $22.8 billion for 2000. As previously indicated, during the second quarter of 2001, we took steps to restructure our investment in Embratel which resulted in the deconsolidation of Embratel effective January 1, 2001. Excluding Embratel from the 2000 period, 2001 commercial services revenues increased 10.9% versus 2000.

Voice revenues for 2001 decreased 6.3% over 2000 on traffic growth of 2.6%. The revenue decreases were partially offset by wireless voice revenue increases of 32.6% for 2001. Excluding wireless voice revenues, commercial voice revenues decreased 12.7% over 2000. Voice revenues include domestic commercial long distance and local switched revenues.

Data revenues for 2001 increased 16.7% over 2000. Data includes both commercial long distance and local dedicated bandwidth sales. For the year ended December 31, 2001, approximately 32% of data revenues were derived from frame relay and asynchronous transfer mode services, where we experienced demand for capacity increases across the product set as businesses moved more of their mission-critical applications to their own networks during the period. At the same time, we continued to experience strong price pressure for data services in our emerging markets due to competition and the general decline in economic condition of our customers, which we expect to continue in the foreseeable future.

International revenues for 2001 increased 25.8% to $3.0 billion versus $2.4 billion, excluding Embratel, for 2000. Geographically, Europe grew 18.4% and Asia Pacific and other areas grew 43.9% for 2001. These increases were partially offset by foreign currency fluctuations that had the effect of reducing revenues by approximately $160 million in 2001. Although our mix improved towards a more profitable blend of data versus voice, and retail versus wholesale, our international business continues to experience significant price pressure on its products.

Internet revenues for 2001 increased 28.7% over 2000. Growth was driven by demand for dedicated circuits as business customers continue to migrate their data networks and applications to Internet-based technologies requiring greater amounts of bandwidth. Additionally, Internet revenues for 2001 included $58 million of Digex revenues, after intercompany eliminations, as a result of the Intermedia merger. During 2001, we began to introduce our new managed hosting products and virtual private networks on public and shared environments. We expect these products, which are in the initial phases of their life cycle, to gradually contribute to our revenue growth over the next several quarters.

Internet revenues include dedicated Internet access, managed networking services and applications (such as virtual private networks), web hosting and electronic commerce and transaction services (such **as** web centers and credit card transaction processing).

Consumer revenues for 2001 decreased 7.1% over 2000. The majority of this decrease is attributed to decreases in calling card, dial around and dial-1 revenues **as** a result of consumers' substitution of wire line services with wireless and e-mail. **Our** consumer local initiatives continued to perform well as consumer local revenues increased approximately 180% for 2001 versus 2000.

Wholesale revenues for 2001 decreased 22.0% over 2000. The wholesale market continued to be extremely price competitive, and this, in addition to bankruptcies, a reduction in private line circuits related to customer internal network consolidation and the impact of the September 11th attacks, contributed to the year-over-year decrease. Wholesale revenues during 2001 were **also** impacted by proactive revenue initiatives, which were made to improve the quality of the wholesale revenue stream **as** we shift the MCI group's focus from revenue growtb to cash generation.

Alternative channcls and small business revenues for 2001 decreased 31.5% over 2000. Alternative channels and small business includes sales agents and affiliates, wholesale alternative channcls, small business, prepaid calling card and wireless messaging revenues. These decreases are attributed to pricing pressures in the wholesale and small business markets which negatively affected revenue growth and gross margins in this area, and proactive initiatives to de-emphasize services with unacceptable gross margins **as** wc shift the MCI group's focus from revenue growth to cash generation.

Dial-up Internet revenues for 2001 decreased 5.7% over 2000. **Our** dial access network has grown 12.7% to approximately 3.2 million modems as of December 31, 2001, compared with the prior year period. Additionally, Internet connect hours increased 9.3% to 7.1 billion hours for 2001 versus 2000. These network usage increases were more than offset by pricing pressure resulting from the impact of volume discounts, which lowered average revenue per hour by approximately 17% for 2001 versus 2000.

Line costs. For the years cndcd December **31,** 2000 and 2001, our line costs were **as** follows (dollars in millions):

	2000		2001	
	$	**Percent of Total**	**$**	**percent of Total**
WorldCom group	$ 8,745	56.6%	$ 8,120	55.1%
MCI **group**	7,117	46.4	7,080	48.0
Intergroup eliminations	(460)	(3.0)	(461)	(3.1)
	$15,462	100.0%	$14,739	100.0%

Line costs **as** a percentage of revenues for 2001 increased to 41.9% **as** compared to 39.6% for 2000. Excluding Embratel for the 2000 period, line costs for 2000 were **$13.8** billion, or 38.9% of revenues. The increase as a percentage of revenues reflects the pricing pressure in the commercial data, international, Internet and wholesale markets as well as the continued competitive pricing in the dial-up Internet business which experienced a 17% decrease in dial-up revenues per hour for 2001 versus 2000. Additionally, line costs **as** a percentage of revenues have increased as a result of the decrease in higner margin calling card and dial around revenues due to wireless substitution **as** noted above.

Line costs were partially offset by foreign currency exchange fluctuations, which had the effect of reducing line costs **as** a percentage of revenues by less than one-half of a percentage point for 2001 as compared to 2000, and by increased data and dedicated Internet traffic over our own facilities, which positively affected line costs as a percentage of revenues by more than one-half **of** a percentage point for 2001.

The principal components of line costs are access charges and transport charges. Regulators have historically permitted access charges to be set at levels that are well above traditional local phone companies' costs. As a result, access charges have been a source of universal service subsidies that enable local exchange rates to be set at levels that are affordable. We have actively participated in a variety of Federal, state, local and international regulatory proceedings with the goal of bringing access charges to cost-based levels and to fund universal service using explicit subsidies funded in a competitively neutral manner. We cannot predict the outcome of these proceedings or whether or not the results will have a material adverse impact on **our** consolidated financial position or results of operations. However, our goal is to manage transport costs through effective utilization of our networks, favorable contracts with carriers and network efficiencies made possible as a result of expansion of our customer base.

Selling, general and administrative. For the years ended December 31, 2000 and 2001, our selling, general and administrative expenses were as follows (dollars in millions):

	2000		2001	
	$	Percent of Total	$	Percent of Total
WorldCom group	$ 5,689	53.7%	$ 6,058	54.8%
MCI group	5,162	48.7	5,348	48.4
Intergroup eliminations	(254)	(2.4)	(360)	(3.2)
	$10,597	100.0%	$11,046	100.0%

Selling, general and administrative expenses for 2001 were $11.0 billion or 31.4% of revenues as compared to $10.6 billion or 27.1% of revenues for 2000. Selling, general and administrative expenses for 2000 include a $685 million pre-tax charge ($340 million from the WorldCom group and $345 million from the MCI group) associated with specific domestic and international wholesale accounts that were deemed uncollectible due to bankruptcies, litigation and scttlcments of contractual disputes that occurrcd in the third quarter of 2000. Additionally, selling, general and administrative expenses for 2000 include a $93 million pre-tax associated with the termination of the Sprint Corporation merger agreement (allocated to the WorldCom group).

Selling, general and administrative expenses for 2001 include pre-tax costs of $865 million ($742 million from the WorldCom group and $123 million from the MCI group) rclated to the write-off of investments in certain publicly traded and privately held companies, $23 million ($12 million from the WorldCom group and $11 million from the MCI group) as a result of the costs associated with the tracking stock capitalization and $207 million associated with domestic and international severance packages and other costs related to our 2001 workforce reductions ($159 million allocated to the WorldCom group and $48 million allocated to the MCI group).

Excluding these charges and Embratel in 2000, selling, general and administrative expenses as a percentage of revenues would have been 28.3% for 2001 versus 25.0% for 2000.

The increase in selling, general and administrative expenses for 2001 includes increased costs associated with "generation d" initiatives, which are designed to position us as a leading supplier of e-business solutions, that include product marketing, customer care, information systems and product development, employee retention costs, and costs associated with multichannel multipoint distribution service product development. Additionally, the increase in selling, general and administrative expenses can be attributed to proactive initiatives to de-emphasize specific wholesale services revenues with unacceptable gross margins which began in the fourth quarter of 2000. These actions resulted in lower revenues, as discussed above, but had no immediate effect on selling, general and administrative expenses for both the wholesale and alternative channels and small business channels.

Selling, general and administrative expenses were offset in part by foreign currency exchange fluctuations which had the effect of reducing selling, general and administrative expenses as a percentage of revenues by almost one-quarter of a percentage point for 2001. Additionally, domestic and international workforce reductions in the first and fourth quarters of 2001, helped to stabilize selling, general and administrative expenses during the remainder of the year.

Depreciation and amortization. For the years ended December 31, 2000 and 2001, our depreciation and amortization expense was as follows (dollars in millions):

	2000		2001	
	$	Percent of Total	$	Percent of Total
WorldCom group	$3,280	67.3%	$4,121	70.1%
MCI group	884	18.1	938	15.9
Intergroup eliminations	714	14.6	821	14.0
	$4,878	100.0%	$5,880	100.0%

Depreciation and amortization expense for 2001 increased to $5.9 billion or 16.7% of revenues from $4.9 billion or 12.5% of revenues for 2000. Excluding Embratel in 2000, depreciation and amortization would have been $4.4 billion or 12.3% of revenues for 2000. These increases reflect additional depreciation associated with 2000 and 2001 capital expenditures as well as increased depreciation associated with the assets acquired in the Intermedia merger. Beginning January 1, 2002, we stopped amortizing intangible assets with indefinite useful lives, including goodwill and tradenames in accordance with SFAS No. 142 "Goodwill and Other Intangible Assets." Based on current levels of such assets, this will reduce our amortization expense by approximately $1.3 billion annually.

Interest expense. Interest expense for 2001 was $1.5 billion or 4.4% of revenues as compared to $970 million or 2.5% of revenues for 2000. Excluding Embratel in 2000, interest expense would have been $1.0 billion or 2.8% of revenues for 2000. For 2000 and 2001, weighted-average annual interest rates on our long-term debt, excluding Embratel in all periods, were 6.93% and 7.29% respectively, while weighted-average levels of borrowings were $20.6 billion and $29.2 billion, respectively. Interest expense for 2001 increased as a result of higher debt levels from the May 2001 bond offering and debt acquired in the Intermedia merger.

Capitalized interest for 2001 was $498 million versus $495 million for 2000. We expect capitalized interest for 2002 to decline by approximately $40-$60 million as a result of lower capital expenditure construction. However, continued debt reduction and interest rate management should partially offset the impact of lower capitalized interest on interest expense for 2002.

Miscellaneous income and expense. Miscellaneous income for 2001 was $412 million or 1.2% of revenues compared to $385 million or 1.0% of revenues for 2000. Miscellaneous income includes investment income, equity in income and losses of affiliated companies, the effects of fluctuations in exchange rates for transactions denominated in foreign currencies, gains and losses on the sale of assets and other non-operating items.

Provision for income tares. The effective income tax rate was 38.7% of incomc before taxes for 2001 and 40% for 2000. See note 9 of our notes to consolidated financial statements for a reconciliation of the statutory federal rate for income taxes to our effective income tax rate.

Cumulative effect of accounting change. During 2000, we adopted SAB 101, which requires certain activation and installation fee revenues to be amortized over the average life of the related service rather than be recognized immediately. Costs directly related to these revenues may also be deferred and amortized over the customer contract life. This adoption resulted in a one-time expense of $85 million, net of income tax benefit of $50 million in the first quarter of 2000.

Net income applicable to common shareholders. For 2001, we reported net income applicable to common shareholders of $1.4 billion as compared to $4.1 billion for 2000.

**Year Ended December 31, 1999 vs.
Year Ended December 31,2000**

For the years ended December 31, 1999 and 2000, our revenues were as follows (dollars in millions):

	1999		2000	
	$	Percent of Total	$	Percent of Total
WorldCom group	$19,736	55.0%	$22,755	58.2%
MCI group	16,172	45.0	16,335	41.8
	$35,908	100.0%	$39,090	100.0%

Reported revenues by category for the years ended December 31, 1999 and 2000 reflect the following changes by category (dollars in millions):

	1999	2000	Percent Change
Commercial semces revenues			
Voice	$ 7,433	$ 7,036	(5.3)
Data	5,830	7,389	26.7
International	1,624	2,367	45.8
Embratel, net	2,772	3,508	26.6
Internet	1,554	2,455	58.0
Total commercial semces revenues	19,213	22,755	18.4
Consumer	7,590	7,778	2.5
Wholesale	3,943	3,388	(14.1)
Alternative channels and small business	3,142	3,541	12.7
Dial-up Internet	1,497	1,628	8.8
Total communications semces revenues	35,385	39,090	10.5
Other	523	—	—
Total	$35,908	$39,090	8.9

Commercial services revenues, which include the revenues generated from commercial voice, data, international and Internet services, for 2000 increased 18.4% to $22.8 billion versus $19.2 billion for 1999.

Voice revenues for 2000 decreased 5.3% over 1999 on traffic growth of 6.4% **as** a result of federally mandated access charge reductions, noted under line costs below, that were passed through to the customer. The revenue decrease was partially offset by local voice revenue increases of 17.4% and wireless voice revenue increases of 104% for 2000. We continued to show significant percentage gains in local and wireless voice services as customers purchased "all-distance" voice services from **us.** However, local revenues and wireless voice revenues are still a relatively small component of total commercial voice revenues. Excluding local and wireless voice revenues, commercial voice services revenues for 2000 decreased 15.2% over 1999.

Data revenues for 2000, increased 26.7% over 1999. The revenue growth for data services was driven by a 32.8% increase in frame relay and asynchronous transfer mode services. As of December 31, 2000, approximately 35% of data revenues were derived from frame relay and asynchronous transfer mode services. We continued to experience strong demand for capacity increases across the product set as businesses moved more of their mission-critical applications to their own networks. Additionally, as of December 31, 2000, our domestic local voice grade equivalents had increased 98% to 65.5 million versus the prior year amount.

International revenues for 2000 increased 45.8% to **$2.4** billion versus $1.6 billion for 1999. This includes a 28% increase in revenues from Europe, and a 119% increase in revenues from Asia and other areas. As of December 31, 2000, we had 21 international facility based city networks versus 17 in 1999. Additionally, during 2000 we added over 5,000 buildings for a total of over 15,000 buildings connected on the international networks.

Embratel revenues for 2000 increased 26.6% to $3.5 billion versus $2.8 billion for 1999 as a result of a higher number of fixed phone lines and cellular devices in service within Brazil.

Internet revenues for 2000 increased 58.0% over 1999. Growth was driven by demand for dedicated circuits as business customers migrated their data networks and applications to Internet-based technologies with greater amounts of bandwidth.

Consumer rcvenues for 2000 increased 2.5% over 1999 as the MCI group's partner marketing programs helped to drive Dial-1 product gains. Consumer revenue growth was impacted by declines in transaction brands and calling card services, which were pressured by increasing wireless substitution, and 10-10-321, which the MCI group no longer actively markets.

Wholesale rcvenues for 2000 decreased 14.1% versus 1999 as a result of price pressure. Wholesale revenues for 2000 were also impacted by proactive fourth quarter 2000 revenue actions which had the effect of reducing wholesale revenues by approximately $90 million in the fourth quarter of 2000. These actions were made to improve the quality of the wholesale revenue stream as we shift the MCI group's focus from revenue growth to cash generation.

Alternative channels and small business revenues for 2000 increased 12.7% over 1999. This increase is primarily attributable to internal growth for wholesale alternative channel voice revenues. We expect that pricing pressures in the wholesale and small business markets will negatively affect revenue growth and gross margins in this area and this level of growth will decline in the foreseeable future as a result of these services being de-emphasized as we shift the MCI group's focus from revenue growth to cash generation.

Dial-up Internet revenue growth for 2000 was 8.8% over 1999. Our dial access network has grown 71% to over 2.8 million modems as of December 31, 2000, compared with 1999. Additionally, Internet connect hours increased 54.8% to 6.5 billion hours for 2000 versus 1999. These network usage increases were offset by pricing pressure on dial-up Internet traffic as a result of contract repricings in the second quarter of 2000, which lowered average revenue per hour by 25% for 2000 versus 1999.

Other revenues which, prior to April 1999, consisted of the operations of SHL Systemhouse Corp. and SHL Systemhouse Co., were $523 million for 1999. SHL provided information technology services including outsourcing, information technology consulting, systems integration, private network management, technology development and applications and systems development. In April 1999, we completed the sale of SHL to Electronic Data Systems Corporation for $1.6 billion.

Line costs. For the years ended December 31, 1999 and 2000, our line costs were as follows (dollars in millions):

	1999		2000	
	$	Percent of Total	$	Percent of Total
WorldComgroup	$ 7,905	53.6%	$ 8,745	56.6%
MCI group	7,087	48.1	7,177	46.4
Intergroup eliminations.	(253)	(1.7)	(460)	(3.0)
	$14,739	100.0%	$15,462	100.0%

Line costs as a percentage of revenues for 2000 decreased to 39.6% as compared to 41.0% for 1999. The overall improvements are a result of increased data and dedicated Internet traffic at the WorldCom group, which positively affected line costs as a percentage of revenues by approximately one percentage point. Additionally, access charge reductions that occurred in January 2000 and July 2000 reduced total line cost expense by approximately $245 million for 2000. While access charge reductions were primarily passed through to customers, line costs as a percentage of revenues were positively affected by almost one half of a percentage point. These improvements were somewhat offset by 2000 contract repricings in our dial-up Internet business as noted above and continued competitive pricing on the dial-up Internet business, which effectively held the average cost per hour constant although average dial-up Internet revenues per hour decreased by 25%.

Selling, general and administrative. For the years ended December 31, 1999 and 2000, our selling, general and administrative expenses were as follows (dollars in millions):

	1999		2000	
	$	Percent of Total	$	percent of Total
WorldCom group..	$4,195	47.0%	$ 5,689	53.7%
MCIgroup	5,071	56.7	5,162	48.7
Intergroup eliminations	(331)	(3.7)	(254)	(2.4)
	$8,935	100.0%	$10,597	100.0%

Selling, general and administrative expenses for 2000 were $10.6 billion or 27.1% of revenues as compared to $8.9 billion or 24.9% of revenues for the year ended December 31, 1999.

Selling, general and administrative expenses for 2000 include a $93 million pre-tax charge associated with the termination of the Sprint Corporation merger agreement, including regulatory, legal, accounting and investment banking fees and other costs, and a $685 million pre-tax charge associated with specific domestic and international wholesale accounts that were no longer deemed collectible due to bankruptcies, litigation and settlements of contractual disputes that occurred in the third quarter of 2000. We maintain general uncollectible reserves based on historical experience, and specific reserves for items such as bankruptcies, litigation and contractual settlements that are established in the period in which the settlement is both estimable and probable. During the third quarter of 2000, an unprecedented number of our wholesale customers either filed for bankruptcy or changed their status in bankruptcy from reorganization to liquidation. This, combined with the third quarter 2000 declines in stock prices for many companies in the telecommunications industry and the overall tightening of the capital markets, which limited the access of many telecommunications providers to the necessary capital to continue operations, led to our specific write-off of such accounts. Prior to the third quarter 2000 events, the general uncollectible reserves were, in our view, adequate. Additionally, under contractual arrangements with traditional local phone companies and other competitive local exchange carriers, we billed the traditional local phone companies and competitive local exchange carriers for traffic originating on the traditional local phone company's or competitive local exchange carrier's networks and terminating on our network. The traditional local phone companies and competitive local exchange carriers have historically disputed these billings, although the collectibility of these billings had continued to be affirmed by public service commission and FCC rulings and by the full payment from a traditional local phone company of the largest past due amount. However, during the third quarter of 2000, court rulings and Congressional discussions led to **our** negotiation and settlement with certain traditional local phone companies and competitive local exchange carriers for these outstanding reccivablcs. Based on the outcome of these negotiations, we recorded a specific provision for the associated uncollectible amounts.

Excluding these charges, selling, general and administrative expenses **as** a percentage of revenues would have been 25.1% for 2000. Selling, general and administrative expenses for 2000 includes increased costs associated with "generation d" initiatives, which are designed **to** position **us as** a leading supplier of e-business solutions, that include product marketing, customer care, information systems and product development, employee retention costs, and costs associated with multichannel multipoint distribution service product development. These increased costs affected selling, general and administrative expense **as** a percentage of revenues by approximately two percentage points.

Depreciation and amortization. **For** the years ended December 31, 1999 and 2000, WorldCom's depreciation and amortization expense was as follows (dollars in millions):

	1999		2000	
	$	Percent of Total	$	percent of Total
WorldCom group.	$3,013	69.2%	$3,280	67.3%
MCI group	757	17.4	884	18.1
Intergroup eliminations	584	13.4	714	14.6
	$4,354	100.0%	$4,878	100.0%

Depreciation and amortization expense for 2000 increased to $4.9 billion or 12.5% of revenues from $4.4 billion or 12.1% of revenues for 1999. This increase primarily reflects additional depreciation associated with increased capital expenditures.

Interest expense. Interest expense for 2000 was $970 million or 2.5% of revenues **as** compared to $966 million or 2.7% of revenues for 1999. For 2000 and 1999, weighted-average annual interest rates on **our** long-term debt were 7.28% and 7.23% respectively, while weighted-average levels of borrowings were $21.6 billion and $19.1 billion, respectively.

Interest expense for 2000 was favorably impacted by increased construction activity and the associated interest capitalization, offset in part by higher weighted-average levels of borrowings and higher interest rates on our variable rate debt and 2000 public debt offerings. Interest expense for 2000 was also favorably impacted **as** a result of **SHL** sale proceeds, investment sale proceeds and proceeds from the increase in our receivables purchase program in the third quarter of 1999 used to repay indebtedness under our credit facilities and commercial paper program.

Miscellaneous ***income and expense.*** Miscellaneous income for 2000 was $385 million **or** 1.0% of revenues **as** compared to $242 million or 0.7% of rcvenues for 1999. Miscellaneous income includes investment income, equity in income and losses of affiliated companies, the effects of fluctuations in exchange rates for transactions denominated in foreign currencies, gains and losses on the sale of assets and other non-operating items.

Provision for income taxes. The effective income tax rate for 2000 was 40.0% of income before taxes. The 2000 rate is greater than the expected federal **statutory** rate of 35% primarily due to the amortization of the non-deductible goodwill. Excluding non-deductible amortization of goodwill, our effective income tax rate would have been 35.0%.

Cumulative effect of accounting change. During the fourth quarter of 2000, we implemented SAB 101, which requires certain activation and installation fee revenues to be amortized over the average life of the related service rather than be recognized immediately. Costs directly related to these revenues may also be deferred and amortized over the customer contract life. As required by SAB 101, wc retroactively adopted this accounting effective January 1, 2000, which resulted in a one-time expense of $85 million, net of income tax benefit of $50 million.

Net income applicable to common shareholders. For the year ended December 31, 2000, we reported net income applicable to common shareholders of $4.1 billion as compared to $3.9 billion for the year ended December 31, 1999.

Athibution and allocation of Assets, Liabilities, Revenues and Expenses between the WorldCom group and the MCI group

The following is a discussion of the methods used to attribute and allocate property and equipment, revenues, line costs, shared corporate services, intangible assets and financing arrangements to the WorldCom group and the MCI group. These methods have been consistently applied for the years ended December 31, 1999, 2000 and 2001. Additionally, our management believes that the cost allocations outlined below are equitable and provide a reasonable estimate of the costs attributable to each group.

Property and equipment. Property and equipment was attributed to the WorldCom group and the MCI group based on specific identification consistent with the assets necessary to support the continuing operations of the businesses attributed to the respective groups. The balances of property and equipment attributed to each of the groups as of December 31, 2001 are as follows:

	WorldCom group	MCI group	Worldcorn
		(in millions)	
Transmission equipment.	$23,369	$ 445	$23,814
Communications equipment.	5,434	2,444	7,878
Furniture, fixtures and other	10,583	680	11,263
Construction in progress	5,576	130	5,706
	44,962	3,699	48,661
Accumulated depreciation	(8,170)	(1,682)	(9,852)
	$36,792	$2,017	$38,809

Revenues. Revenues have been attributed to the WorldCom group and the MCI group based on specific identification of the lines of business that are attributed to the two groups.

Line costs. Allocated line costs and related liabilities include the costs of the fiber optic systems attributed to the WorldCom group and the costs of the business voice switched services attributed to the MCI group. Line costs have been attributed to the WorldCom group and the MCI group predominantly based on specific identification of network usage by that group. Where determinations based on specific usage alone were impractical, we used other allocation methods, including methods based on the total revenues generated by each group.

Shared corporate services. A portion of our shared corporate services and related balance sheet amounts (such as executive management, human resources, legal, regulatory, accounting, tax, treasury, strategic planning and information systems support) has been attributed to the WorldCom group or the MCI group based upon identification of such services specifically benefiting such group. Where determinations based on specific usage alone have been impractical, we used other allocation methods that we believe are fair, including methods based on such factors as the number of employees and total line costs or revenues generated by each group.

Allocation of intangible assets. Intangible assets include the excess consideration paid over the fair value of net tangible assets acquired by us in business combinations accounted for under the purchase method and include goodwill, channel rights, developed technology and tradenames. These assets have been attributed to the respective groups based on specific identification and where acquired companies have been divided between the WorldCom group and the MCI group, the intangible assets have been allocated based on the respective fair values at the date of purchase of the related operations attributed to each group. Our management believes that this method of allocation is equitable and provides a reasonable estimate of the intangible assets attributable to the WorldCom group and the MCI group.

All tradenames, including the MCI tradename and the other related MCI tradenames, have been attributed to the WorldCom group. The MCI group will be allocated an expense, and the WorldCom group will he allocated a corresponding decrease in depreciation and amortization expense, for the use of the MCI tradcnamcs for the next four years based on the following schedule:

2002: $30.0 million
2003: $35.0 million
2004 $40.0 million
2005: $45.0 million

Any renewal or termination of use of the MCI tradename by the MCI group will be subject to the general policy that our board of directors will act in the best interests of WorldCom. For each of the years ended December 31, 1999, 2000 and 2001, depreciation and amortization expense associated with the MCI tradenames allocated to the WorldCom group was decreased by $27.5 million per annum for use of the MCI tradenames by the MCI group.

Goodwill and other intangibles assigned or allocated to the WorldCom group and the MCI group as of December 31, 2001 are as follows:

	Worldcorn group	MCI group	WorldCom
	(in millions)		
Goodwill	$40,551	$ 9,274	$49,825
Tradenames	1,112	—	1,112
Developed technology	1.590	510	2,100
Other intangibles	3,414	1,443	4,857
	46,667	11,227	57,894
Accumulated amortization	(5,849)	(1,508)	(7,357)
	$40,818	$ 9,719	$50,537

Financing arrangements. As of January 1, 1999, $6.0 billion of our outstanding debt was notionally allocated to the MCI group and the remainder of our debt was notionally allocated to the WorldCom group. Our debt was allocated between the WorldCom group and the MCI group based upon a number of factors including estimated future cash flows and the ability to pay debt service and dividends of each of the groups. In addition, management considered certain measures of creditworthiness, such as coverage ratios and various tests of liquidity, in the allocation process. Our management believes that the initial allocation was equitable and supportable by both the WorldCom group and the MCI group. The debt allocated to the MCI group bears interest at a rate indicative of the rate at which the MCI group would borrow from third parties if it was a wholly owned subsidiary of WorldCom but did not have the benefit of any guarantee by WorldCom. Interest rates will be calculated on a quarterly basis. Debt allocated to the MCI group bears an interest rate equal to the weighted-average interest rate, excluding capitalized interest, of WorldCom debt plus 1¼ percent. Interest allocated to the WorldCom group reflects the difference between our actual interest expense and the interest expense charged to the MCI group. Subsequent to the recapitalization, each group's allocated debt increases or decreases by the amount of any net cash gencratcd by, or required to fund, the group's operating activities, investing activities, dividend payments, share repurchases and other financing activities.

As of December 31, 2001, our receivables purchase program consisted of a $3.7 billion pool of receivables in which the purchaser owned an undivided interest, including $2.0 billion sold. The WorldCom group was allocated $2.8 billion of the pool and $1.7 billion of the sold receivables. The MCI group was allocated the balance. The receivables sold were assigned based on specific identification where practical, or allocated based on total revenues. **Our** management believes that this method of allocation is equitable and provides a reasonable estimate of the receivables attributable to the groups.

WorldCom Group** Results of **Operations

The following table sets forth for the periods indicated the WorldCom group's statements of operations in millions of dollars and as a percentage of its revenues for the periods indicated:

	For the Years Ended December 31,					
	1999		2000		2001	
Revenues	$19,736	100.0%	$22,755	100.0%	$21,348	100.0%
Line costs	7,905	40.1	8,745	38.4	8,120	38.0
Selling, general and administrative	4,195	21.3	5,689	25.0	6,058	28.4
Depreciation and amortization	3,013	15.3	3,280	14.4	4,121	19.3
Other charges	(8)	—	—	—	—	—
Operating income	4.631	23.5	5,041	22.2	3,049	14.3
Other income (expense):						
Interest expense	(460)	(2.3)	(458)	(2.0)	(1,029)	(4.8)
Miscellaneous	237	1.2	385	1.7	412	1.9
Income before income taxes, minority interests and cumulative effect of accounting change	4,408	22.3	4,968	21.8	2,432	11.4
Provision for income taxes	1,856	9.4	1,990	8.7	943	4.4
Income before minority interests and cumulative effect of accounting change	2,552	12.9	2,978	13.1	1,489	7.0
Minority interests	(186)	(0.9)	(305)	(1.3)	35	0.2
Cumulative effect of accounting change	—	—	(75)	(0.3)	—	—
Distributions on other mandatorily redeemable preferred securities and other preferred dividend requirements	72	0.4	65	0.3	117	0.5
Net income..	$ 2.294	11.6%	$ 2,533	11.1%	$ 1,407	6.6%

Year Ended December 31, 2000 vs.
Year Ended December 31, 2001

Revenues. Reported revenues by category for 2000 and 2001 reflect the following changes by category (dollars in millions):

	2000	2001	Percent Change
Commercial services revenues			
Voice..	$ 7,036	$ 6,591	(6.3)%
Data	7,389	8,620	16.7
International	2,367	2,977	25.8
Embratel, net	3,508	—	(100.0)
Internet	2,455	3,160	28.7
Total commercial services revenues	$22,755	$21,348	(6.2)

WorldCom group rcvenues for 2001 were $21.3 billion versus $22.8 billion for 2000. As previously indicated, during the second quarter of 2001, we took steps to restructure our investment in Embratel which resulted in the deconsolidation of Embratel effective January 1, 2001. Excluding Embratel from the 2000 periods, WorldCom group revenues for 2001 increased 10.9% versus 2000.

Voice revenues for 2001 decreased 6.3% over 2000 on traffic growth of 2.6%. The revenue decreases were partially offset by wireless voice revenue increases of 32.6% for 2001. Excluding wireless voice revenues, commercial voice revenues decreased 12.7% over 2000.

Data revenues for 2001 increased 16.7% over 2000. For the year ended December 31, 2001, approximately 32% of data revenues were derived from frame relay and asynchronous transfer mode services, where we experienced demand for capacity increases across the product set as businesses moved more of their mission-critical applications to their own networks during the period. At the same time, we continued to experience strong price pressure for data services in our emerging markets due to competition and the general decline in economic condition of our customers, which we expect to continue in the foreseeable future.

International revenues for 2001 increased 25.8% to $3.0 billion versus $2.4 billion, excluding Embratel, for 2000. Geographically, Europe grew 18.4% and Asia Pacific and other areas grew 43.9% for 2001. These increases were partially offset by foreign currency fluctuations that had the effect of reducing revenues by approximately $160 million in 2001. Although our mix improved towards a more profitable blend of data versus voice, and retail versus wholesale, our international business continues to experience significant price pressure on its products.

Internet revenues for 2001 increased 28.7% over 2000. Growth was driven by demand for dedicated circuits as business customers continue to migrate their data networks and applications to Internet-based technologies requiring greater amounts of bandwidth. Additionally, Internet revenues for 2001 included $58 million of Digex revenues, net of intercompany eliminations, as a result of the Intermedia merger. During 2001, we began to introduce our new managed hosting products and virtual private networks on public and shared environments. We expect these products, which are in the initial phases of their life cycle, to gradually contribute to our revenue growth over the next several quarters. Internet revenues include dedicated Internet access, managed networking services and applications (such as virtual private networks), web hosting and electronic commerce and transaction services (such as web centers and credit card transaction processing).

Line costs. Line costs as a percentage of revenues for 2001 decreased to 38.0% as compared to 38.4% reported for 2000. Excluding Embratel in 2000, line costs would have been $7.1 billion, or 37.0% of revenues for 2000. The increase as a percentage of revenues excluding Embratel, reflects the pricing pressure in the data, international and Internet markets. Line costs were partially offset by foreign currency exchange fluctuations which had the effect of reducing line costs as a percentage of revenues by more than one-half of a percentage point for 2001, and by increased data and dedicated Internet traffic over our own facilities, which positively affected line costs as a pcrccntage of revenues by almost three-fourths of one percentage point for 2001.

Selling, general and administrative. Selling, general and administrative expenses for 2001 were $6.1 billion or 28.4% of revenues as compared to $5.7 billion or 25.0% of revenues for the prior year period. Selling, general and administrative expenses for 2000 include a $340 million pre-tax charge associated with specific domestic and international wholesale accounts that were deemed uncollectible due to bankruptcies, litigation and settlements of contractual disputes that occurred in the third quarter of 2000 and a $93 million pre-tax charge associated with the termination of the Sprint Corporation merger agreement. Selling, general and administrative expenses for 2001 include pre-tax costs of $742 million related to the write-off of investments in certain publicly traded and privately held companies, $12 million as a result of the costs associated with the tracking stock capitalization and $159 million associated with domestic and international severance packages and other costs related to our 2001 workforce reductions. Excluding these charges and Embratel in 2000, selling, general and administrative expenses as a percentage of revenues would have been 24.1% for 2001 versus 22.5% for 2000.

The increase in selling, general and administrative expenses **for** 2001 includes increased costs associated with "generation d" initiatives that include product marketing, customer care, information system and product development, employee retention costs, and costs associated with multichannel multipoint distribution service product development.

Selling, general and administrative expenses were offset in part by foreign currency exchange fluctuations which had the effect of reducing selling, general and administrative expenses as a percentage of revenues by less than one-half of a percentage point for 2001. Additionally, domestic and international workforce reductions in the first and fourth quarters of 2001 helped to stabilize selling, gencral and administrative costs during the remainder of the year.

Depreciation and amortization. Depreciation and amortization expense for 2001 increased to $4.1 billion or 19.3% of revenues from **$3.3** billion or 14.4% of revenues for 2000. Excluding Embratel in 2000, depreciation and amortization would have been $2.8 billion or 14.5% of revenues for 2000. The increase reflects increased depreciation associated with 2000 and 2001 capital expenditures as well as increased depreciation associated with the assets acquired in the Intermedia merger. Beginning January 1, 2002, the WorldCom group stopped amortizing intangible assets with indefinite useful lives, including goodwill and tradenames in accordance with SFAS No. 142. Based on current levels of such assets, this will reduce the WorldCom group's amortization expense by approximately $1.0 billion annually.

Interest expense. Interest expense for 2001 was $1.0 billion or 4.8% of revenues **as** compared to $458 million or 2.0% of revenues for 2000. Excluding Embratel in 2000, interest expense would have been $502 million, or 2.6% of revenues for 2000. Interest expense on borrowings incurred by WorldCom and allocated to the WorldCom group reflects the difference between WorldCom's actual interest expense and the interest expense allocated to the **MCI** group. The MCI group was allocated interest based on the weighted-average interest rate, excluding capitalized interest, of WorldCom debt plus 1% percent.

Capitalized interest for 2001 was $498 million versus $495 million for 2000. We expect capitalized interest for 2002 to decline by approximately $40–$60 million as a result of lower capital expenditure construction. However, continued debt reduction and interest rate management should partially offset the impact of lower capitalized interest on interest expense for 2002.

Miscellaneous Income and Expense. Miscellaneous income for 2001 was $412 million, or 1.9% of revenues as compared to $385 million, or 1.7% of revenues for 2000. Miscellaneous income includes investment income, equity in income and losses of affiliated companies, the effects of fluctuations in exchange rates for transactions denominated in foreign currencies, gains and losses on the sale of assets and other non-operating items.

Provision for Income Taxes. The effective income tax rate was 38.8% of income before taxes for 2001 and 40.1% for 2000. See note 10 to the WorldCom group's combined financial statements for a reconciliation of the statutory federal rate for income taxes to the WorldCom group's effective income tax rate.

Cumulative Effect of Accounting Change. During 2000, we adopted SAB 101, which requires certain activation and installation fee revenues to be amortized over the average life of the related service rather than be recognized immediately. Costs directly rclated to these revenues may also be deferred and amortized over the customer contract life. This adoption resulted in a one-time expense of $75 million, net of income tax benefit of $43 million, for the WorldCom group in the first quarter of 2000.

Net Income. For 2001, the WorldCom group reported net income of $1.4 billion as compared to $2.5 billion for 2000. Pro forma diluted income per common share for 2001 was $0.48 compared to incomc per common share of $0.87 for 2000. Pro forma diluted income per share assumes the recapitalization occurred at the beginning of 2000 and that the WorldCom group stock and MCI group stock existed for all periods presented.

**Year Ended December 31, 1999 vs.
Year Ended December 31,2000**

Revenues. Revenues for 2000 increased 15.3% to $22.8 billion versus $19.7 billion for 1999. The increase in total revenues is attributable to internal growth of the WorldCom group.

Reported revenues by category for the years ended December 31, 1999 and 2000 reflect the following changes by category (dollars in millions):

	1999	2000	Percent Change
Commercial services revenues			
Voice	$ 7,433	$ 7,036	(5.3)
Data	5,830	7,389	26.7
International	1,624	2,367	45.8
Embratel, net	2,772	3,508	26.6
Internet	1,554	2,455	58.0
Total commercial services revenues	19.213	22.755	18.4
Other	523	—	—
Total	$19,736	$22,755	15.3

Voice revenues for 2000 decreased 5.3% over 1999 on traffic growth of 6.4% as a result of federally mandated access charge reductions, noted under line costs below, that were passed through to the customer. The revenue decrease was partially offset by local voice revenue increases of 17.4% and wireless voice revenue increases of 104% for 2000. We continued to show significant percentage gains in local and wireless voice services as customers purchased "all-distance" voice services from us. However, local revenues and wireless voice revenues are still a relatively small component of total commercial voice revenues. Excluding local and wireless voice revenues, commercial voice services revenues for 2000 decreased 15.2% over 1999.

Data revenues for 2000, increased 26.7% over 1999. The revenue growth for data services was driven by a 32.8% increase in frame relay and asynchronous transfer mode services. As of December 31, 2000, approximately 35% of data revenues were derived from frame relay and asynchronous transfer mode services. We continued to experience strong demand for capacity increases across the product set as businesses moved more of their mission-critical applications to their own networks. Additionally, as of December 31, 2000, our domestic local voice grade equivalents had increased 98% to 65.5 million versus the prior year amount.

International revenues for 2000 increased 45.8% to $2.4 billion versus $1.6 billion for 1999. This includes a 28% increase in revenues from Europe, and a 119% increase in revenues from Asia and other areas. As of December 31, 2000, we had 21 international facility based city networks versus 17 in 1999. Additionally, during 2000 we added over 5,000 buildings for a total of over 15,000 buildings connected on the international networks.

Embratel revenues for 2000 increased 26.6% to $3.5 billion versus $2.8 billion for 1999 as a result of a higher number of fixed phone lines and cellular devices in service within Brazil.

Internet revenues for 2000 increased 58.0% over 1999. Growth was driven by demand for dedicated circuits as business customers migrated their data networks and applications to Internet-based technologies with greater amounts of bandwidth.

Other revenues which, prior to April 1999, consisted of the operations of SHL, were $523 million for 1999. In April 1999, we completed the sale of SHL to Electronic Data Systems for $1.6 billion.

Line costs. Line costs as a percentage of revenues for 2000 decreased to 38.4% as compared to 40.1% reported for 1999. The overall improvement is a result of increased data and dedicated Internet traffic over WorldCom-owned facilities, which positively affected line costs as a percentage of revenues by approximately one and one-half percentage points. Additionally, access charge reductions that occurred in January 2000 and July 2000 reduced total line cost expense by approximately $95 million for 2000. While access charge reductions were primarily passed through to customers, line costs as a percentage of revenues were positively affected by more than a quarter of a percentage point.

Selling, general and administrative. Selling, general and administrative expenses for 2000 were $5.7 billion or 25.0% of revenues as compared to $4.2 billion or 21.3% of revenues for 1999. Selling, general and administrative expenses for 2000 include a $340 million pre-tax charge associated with specific accounts that were deemed uncollectible due to bankruptcies, litigation and settlements of contractual disputes that occurred in the third quarter of 2000, and a $93 million pre-tax charge associated with the termination of the Sprint Corporation merger agreement, including regulatory, legal, accounting and investment banking fees and other costs. Excluding these charges, selling, general and administrative expenses as a percentage of revenues were 23.1% for 2000. Selling, general and administrative expenses for 2000 includes increased costs associated with "generation d" initiatives that include product marketing, customer care, information system and product development, employee retention costs, and costs associated with multichannel multipoint distribution service product development. These increased costs affected selling, general and administrative expense as a percentage of revenues by approximately three percentage points.

Depreciation and amortization. Depreciation and amortization expense for the year ended December 31, 2000 increased to $3.3 billion or 14.4% of revenues from $3.0 billion or 15.3% of revenues for 1999. This increase reflects increased depreciation associated with increased capital expenditures. As a percentage of revenues, these costs decreased due to the higher revenue base.

Interest expense. Interest expense for 2000 was $458 million or 2.0% of revenues **as** compared to $460 million or 2.3% of revenues for 1999. Interest expense on borrowings incurred by WorldCom and allocated to the WorldCom group reflects the difference between WorldCom's actual interest expense and the interest expense allocated to the MCI group. The MCI group was allocated interest based on the weighted-average interest rate, excluding capitalized interest, of WorldCom debt plus **1¼** percent.

Miscellaneous income and expense. Miscellaneous income **for** 2000 was $385 million or 1.7% of revenues **as** compared to $237 million or 1.2% of revenues for 1999. Miscellaneous income includes investment income, equity in income and losses of affiliated companies, the effects of fluctuations in exchange rates for transactions denominated in foreign currencies, gains and losses on the sale of assets and other non-operating items.

Provision for income taxes. The effective income tax rate for 2000 was 40.1% of income before taxes. The 2000 rate is greater than the expected federal statutory rate of 35% primarily due to the amortization of the non-deductible goodwill. Excluding non-deductible amortization of goodwill, the WorldCom group's effective income tax rate would have been 34.1%.

Cumulative effect of accounting change. During the fourth quarter of 2000, we implemented **SAB** 101, which requires certain activation and installation fee revenues to be amortized over the average life of the related service rather **than** be recognized immediatcly. Costs directly related to these revenues may **also** be deferred and amortized over the customer contract life. **As** required by **SAB** 101, we retroactively adopted this accounting effective January 1, 2000, which resulted in a one-time expense of $75 million, net of income tax benefit of $43 million for the WorldCom group.

Net income. **For** the year ended December 31, 2000, the WorldCom group reported net income of $2.5 billion **as** compared to $2.3 billion for the year ended December 31, 1999.

MCI Group Results of Operations

The following table sets forth for the periods indicated the MCI group's statements of operations in millions of dollars and **as a** percentage of its revenues for the periods indicated

	For the Years Ended December 31,					
	1999		2000		2001	
Revenues	$16,172	100.0%	$16,335	100.0%	$13,831	100.0%
Line costs	7,087	43.8	7,177	43.9	7,080	51.2
Selling, general and administrative	5,071	31.4	5,162	31.6	5,348	38.7
Depreciation and amortization	757	4.7	884	5.4	938	6.8
Operating income	3,257	20.1	3,112	19.1	465	3.4
Other income (expense):						
Interest expense	(506)	(3.1)	(512)	(3.1)	(504)	(3.6)
Miscellaneous	5	—	—	—	—	—
Income (loss) before income taxes and cumulative effect of accounting change	2,756	17.0	2,600	15.9	(39)	(0.3)
Income tax expense (benefit)	1,109	6.9	1,035	6.3	(16)	(0.1)
Income (loss) before cumulative effect of accounting change	1,647	10.2	1,565	9.6	(23)	(0.2)
Cumulative effect of accounting change	—	—	(10)	(0.1)	—	—
Net income (loss)	$ 1,647	10.2%	$ 1,555	9.5%	$ (23)	(0.2)%